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DATE: September 11, 2014

TO: Committee Financial Liability Reform  
Chair Earl Poleski

FROM: City of Owosso  
Benjamin R. Frederick, mayor  
Donald D. Crawford, city manager  
Richard C. Williams, finance director

SUBJECT: House Bill 5279 amending MCL. 141.2518(10) Public Act 34 of 2001 adding section 518  
(MCL 141.2518) by Public Act 329 of 2012

#### INTRODUCTION:

As this committee considers SB 922, we appreciate members taking a few minutes to consider an urgent need for the City of Owosso and other communities which is addressed within House Bill 5279 and which amends the same underlying statute.

The city of Owosso supports HB 5279 allowing communities with an underlying credit rating of A or higher or the equivalent assigned by a nationally-recognized rating agency to bond for pension obligations. HB 5279 also requires A-rated communities to provide credit enhancement in the form of bond insurance, which provides additional security and a secondary source of payment. Providing insurance on a bond offering improves the credit quality of the issue, resulting in an upgrade to the underlying credit rating. Owosso supports this provision as well.

The city of Owosso meets all the requirements of section 518 except for criteria found in paragraph 10 requiring a municipality to be assigned a credit rating of AA or higher or the equivalent by at least one nationally-recognized rating agency. When one looks at the rating criteria, Owosso is highly rated with respect to financial condition, management practices of the governing body and administration, and debt structure. The city loses because of demographic factors (age of residents, income of residents, housing values and ability to grow physically) and economy (rural, employments, lack of diverse manufacturing, and simply being in Michigan).

#### BACKGROUND:

The city of Owosso closed its defined benefit retirement program to all new entrants in July 2006.

The effect of closing a defined benefit plan accelerates the amortization of the unfunded liabilities, driving up the annual required contribution. Owosso's annual contributions have moved from \$390,599 in 2010 to \$808,515 in 2014. This level of contribution is expected to continue for the next 15 years and impairs the city's ability to fund general operations like public safety.

The city's pension plan is funded at 89.1% with an unfunded actuarially accrued liability (UAAL) of \$3,907,813. With passage of HB 5279, the city would bond for the UAAL and provide the proceeds to the retirement system to be invested. The relief to general purpose general operations is provided by the expected spread between the net interest cost of the bond offering and the investment returns of the retirement system. Past investment returns are not guaranteed but historical average returns provide a very comfortable margin between the borrowing rate and the investment rate.

Owosso has three pension plans. First is the City of Owosso Employee Pension Plan, covering most employees employed before 2006 and current fire and police officers. Second is the MERS plan that covers the police command. Third are defined contribution plans covering employees (except fire and police) employed after 2006.

The plan we are currently concerned with is the City of Owosso Employee Pension Plan. For many years, the city made no contribution, as the actuarial projections showed that it was over funded. Then in 2006 (AFSCME implemented 7/1/2005) the plan was closed to new employees, which meant that no younger employees would be contributing and that the age of member employees would continue to increase--the average age is now 51.7 years. Then came the 2008 market crash, and the fund lost \$11,108,104 in value while the number of employees retiring increased (four in 2009, five in 2010, eight in 2011, four in 2012, six in 2013). In addition, the city permanently laid off five employees. Thus, new actuarial studies showed that the mandated city contribution had to increase as follows:

2010--	\$390,599
2011--	\$550,684
2012--	\$829,038
2013--	\$701,388
2014--	\$808,515
2015--	\$810,348

The ability to bond would reduce the annual amount by about 50% or \$400,000 annually for the next 15 years.

#### CONCLUSION:

Owosso has been fiscally prudent by closing the defined benefit pension plans and moving to defined contribution plans. The city does not offer post-employment benefits like health insurance. Because of this prudence, the city is penalized by being unable to restructure the pension liability created in a past day when the city and state were thriving, resulting in reduced services to city residents.

We urge that this tool be made available by the state so that Owosso and other communities can prudently address these liabilities with NO risk to taxpayers and without threatening core services.